

## Message Text

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ACTION FS-01

INFO OCT-01 ISO-00 /002 W

----- 017538

R 040817Z SEP 74

FM AMEMBASSY PARIS

TO SECSTATE WASHDC 1986

LIMITED OFFICIAL USE SECTION 1 OF 2 PARIS 20854

STATE FOR BF/FMS ATTN MR. GULLI

FOLLOWING ROME 11865 SENT ACTION TO 40TH TAC GP FAF AVIANO  
6917 RSM BRINDISI COMSIXTHFLT GAETA USCINCEUR VAIHINGEN  
DIVENGR USAEDM LEGHORM NAVSUPPACT NAPLES AMEMBASSY PARIS  
NAF SIGONELLA COMPTROLLER USASETAF VICENZA ON AUG 29, 1974  
REPEATED FOR YOUR INFO

QUOTE

LIMITED OFFICIAL USE ROME 11865

PARIS FOR RFC

E.O. 11652: N/A

TAGS: EFIN, IT

SUBJECT: US MILITARY FINANCE OFFICER'S MEETING IN ROME SEPTEMBER  
16, 1974

FOLLOWING IS REPEATED FOR YOUR INFORMATION IN CONNECTION  
WITH SUBJECT MEETING. ADDITIONAL BACKGROUND INFO BEING MAILED.

FOLLOWING SENT BY AMEMBASSY ROME TO SECSTATE, AMEMBASSY  
PARIS, USCINCEUR VAIHINGEN/ECCM ON MAY 23, 1974. H/W REPEATED  
FOR YOUR INFO:

LIMITED OFFICIAL USE ROME 7116

FOR DEFENSE, TREASURY (PASS FISCAL SERVICE COX), PARIS RFC  
FOR LERCHBAUM  
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E.O. 11652: N/A

TAGS: EFIN, IT

SUBJECT: RENEGOTIATION OF ARRANGEMENT ON EXCHANGE RATE AND LIRA  
PURCHASES OF US GOVERNMENT IN ITALY

REF: (A) ROME 3991 OF MARCH 22, 1974

(B) ROME 3136 OF MARCH 6, 1974

(C) ROME 1651 OF FEBRUARY 5, 1974

1. SUMMARY. DUE TO UNIFICATION OF ITALIAN DUAL EXCHANGE MARKET ON MARCH 22 (REPORTED REF A), OUR PROPOSED PROCEDURE TO OBTAIN FOREIGN BANKNOTE VERSION OF FORMER FINANCIAL LIRA RATE FOR US\$ LIRE PURCHASES IS NO LONGER VIABLE (SEE REF B). NEVERTHELESS WE BELIEVE THAT SPECIAL ARRANGEMENT BETWEEN US\$ AND GOI CONCERNING EXCHANGE RATE FOR US\$ EXPENDITURES IN ITALY SHOULD BE PRESERVED. WE THEREFORE PROPOSE THAT WE PROCEED WITH EXCHANGE OF LETTERS BETWEEN AMBASSADOR AND ITALIAN TREASURY MINISTER. INFORMAL APPROVAL OF NEW DRAFT TEXT OF PROPOSED LETTER AND OF ANNEX HAS BEEN RECEIVED FROM BANK OF ITALY, EXCHANGE OFFICE, FOREIGN TRADE AND TREASURY MINISTRIES. REQUEST APPROVAL BY WASHINGTON AGENCIES OF TEXT OF ARRANGEMENT, SO THAT EXCHANGE OF LETTERS CAN BE MADE. END SUMMARY.

2. ALTHOUGH LEGAL RATE STILL EXISTS FOR FOREIGN BANKNOTES, IT HAS BEEN ONLY TWO TO SEVEN LIRE MORE FAVORABLE THAN NEW OFFICIAL RATE AND RECENTLY HAS OCCASIONALLY BEEN LESS FAVORABLE. THIS DIFFERENCE PROVIDES INSUFFICIENT INCENTIVE TO ESTABLISH COMPLEX SYSTEM PREVIOUSLY CONSIDERED, SINCE IT WAS PREDICATED ON MUCH LARGER SPREAD (SEE REF C). IN ANY CASE, NEW ARRANGEMENT WOULD PROVIDE POSSIBILITY OF BUYING LIRE FROM BOI EITHER AT ORDINARY RATE OR AT FOREIGN BANKNOTE RATE (LESS 9.1 PERCENT SHIPMENT FEE). RATHER THAT SUSPEND DISCUSSIONS WITH GOI ALTOGETHER, WE PROPOSE TO PROCEED WITH EXCHANGE OF LETTERS BETWEEN AMBASSADOR AND ITALIAN MINISTER OF TREASURY.

3. WE RECOGNIZE THAT FINANCIAL INCENTIVE FOR INTRODUCING LIMITED OFFICIAL USE

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NEW ARRANGMENT TO REPLACE OLD TASCA AGREEMENT HAS BEEN ELIMINATED AS RESULT OF UNIFICATION OF EXCHANGE RATES AND THAT PRESENT MORE LIMITED PROPOSAL HAS BOTH ADVANTAGES AND DISADVANTAGES. HOWEVER, WE BELIEVE THAT FORMER OUTWEIGH LATTER. ADVANTAGES ARE: (1) MAINTAINING CONTINUITY IN SPECIAL US\$/GOI EXCHANGE RATE ARRANGEMENTS; (2) TERMINATING SOME RECENT EXCHANGE OPERATIONS BY US\$ AGENCIES WHICH COULD PROVE EMBARRASSING

FOR USG/GOI RELATION; AND (3) PROVIDING DIRECT EVIDENCE IN GOI'S OWN STATISTICS OF AT LEAST PART OF USG MILITARY EXPENDITURES IN ITALY FOR BURDEN-SHARING PURPOSES.

4. SUBSTITUTION OF NEW PROCEDURAL ARRANGEMENT FOR 1947 TASCA AGREEMENT WOULD INFORMALLY RECONFIRM COMMITMENT OF GOI TO GRANT USG SPECIAL AND FAVORABLE EXCHANGE RATE ARRANGEMENTS. ALTHOUGH ADVANTAGES OF USG OF MAINTAINING SPECIAL ARRANGEMENT MAY NOT APPEAR VERY GREAT AT PRESENT, WE BELIEVE THAT, GIVEN POSSIBILITY OF FURTHER CHANGES IN ITALIAN EXCHANGE REGIME, ARRANGEMENT COULD PROVE TO BE OF VALUE AT SOME FUTURE TIME.

5. PROPOSED REVISED PROCEDURES (ANNEX APPENDED TO AMBASSADOR'S LETTER) ARE INTENDED TO RETURN TO ORIGINAL TASCA AGREEMENT INTENT, SO AS TO REQUIRE ALL OFFICIAL LIRE PURCHASES TO BE MADE EXCLUSIVELY FROM BRANCHES OF BANK OF ITALY. DURING EXISTENCE OF DUAL MARKET, MILITARY DISBURSING OFFICERS WERE PERMITTED TO PURCHASE LIRE FROM BANKS AND OTHER AUTHORIZED EXCHANGE DEALERS TO OBTAIN BEST RATE AVAILABLE, PROVIDED THAT TRANSACTIONS WERE LEGAL UNDER ITALIAN EXCHANGE REGULATIONS. DURING PAST YEAR, WE HAVE BECOME AWARE THAT TRANSACTIONS OF QUESTIONABLE PROPRIETY WERE BEING MADE. PURCHASING OF LIRE FOR US GOVERNMENT AGENCIES' NEEDS EXCLUSIVELY FROM GOI WOULD PRECLUDE OCCURRENCE OF TRANSACTIONS WHICH MAY BE FEEDING BLACK MARKET AND CONTRAVENING INTENT OF ITALIAN EXCHANGE CONTROLS. DIRECT LIRA PURCHASES FROM BOI WOULD ALSO PROVIDE RECORD IN BANK OF ITALY'S OWN STATISTICS OF PART OF US MILITARY EXPENDITURES IN ITALY FOR BALANCE OF PAYMENTS BURDEN-SHARING PURPOSES.

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6. RESTRICTING ALL USG LIRE PURCHASES IN ITALY TO BOI WOULD ALSO MEAN THAT RFC PARIS WOULD NO LONGER BE ABLE TO PURCHASE LIRE FROM OTHER SOURCES FOR USE IN ITALY. WE UNDERSTAND THAT ACCORDING TO SECTION 33.3 OF DEPARTMENT OF STATE MANUAL (4 FAM), WHERE STATE AND TREASURY HAVE APPROVED USE OF A SPECIAL RATE, THAT SPECIAL RATE, RATHER THAN PREVAILING MARKET RATE, IS USED. OUR RECORDS SHOW THAT EXCHANGE RATE AVAILABLE TO RFC OUTSIDE ITALY HAS SELDOM BEEN SIGNIFICANTLY HIGHER THAN OFFICIAL RATE INSIDE ITALY. DURING PERIOD MARCH 20, 1973 TO MAY 21, 1974, MAXIMUM SPREAD WAS 9 LIRE PER DOLLAR, WHICH OCCURED ON ONLY TWO OCCASIONS. ON ONLY 16 DAYS IN PERIOD OF MORE THAN ONE YEAR DID OUTSIDE RATE EXCEED RATE IN ITALY BY 4 LIRE OR MORE.

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7. CHIEF DISADVANTAGE OF PROPOSAL WOULD BE TERMINATION OF SOME RECENT LIRA PURCHASES BY USG AGENCIES AT VERY FAVORABLE EXCHANGE RATES. THESE OPERATIONS WERE POSSIBLE BECAUSE AUTHORIZED EXCHANGE DEALERS WERE RE-SELLING DOLLARS ILLEGALLY TO ITALIANS FOR ILLICIT CAPITAL EXPORTS. WE RECOGNIZE THAT IT IS NOT RESPONSIBILITY OF USG TO ATTEMPT TO ENFORCE ITALIAN EXCHANGE CONTROLS. ON OTHER HAND, WE ARE TROUBLED BY OPERATIONS BY US GOVERNMENT AGENCIES WHICH CLEARLY HAVE EFFECT OF UNDERCUTTING FINANCIAL POLICIES OF FRIENDLY GOVERNMENT. WE WOULD LIKE TO POINT OUT THAT HIGH EXCHANGE RATES AVAILABLE FROM SOME EXCHANGE DEALERS DO NOT REFLECT ANY GOI POLICY TO MAINTAIN ARTIFICIALLY OVERVALUED OFFICIAL EXCHANGE RATE, AS IS SOMETIMES TRUE IN OTHER PARTS OF WORLD. HIGH RATES DO REFLECT PREMIUM WHICH SOME ITALIANS ARE PREPARED TO PAY IN ORDER TO EXPORT CAPITAL ILLEGALLY FOR VARIETY OF POLITICAL, INCOME YIELD, CURRENCY SPECULATION AND TAX EVASION REASONS. ALTHOUGH ILLEGAL CAPITAL EXPORTS IN ABSOLUTE TERMS ARE FAIRLY LARGE, VOLUME OF SUCH TRANSACTIONS AT BLACK MARKET RATES IS STILL SMALL RELATIVE TO VOLUME OF TRANSACTIONS THAT TAKE PLACE THROUGH OFFICIAL EXCHANGE MARKET.

8. WE HAVE LIMITED THE APPLICABILITY OF NEW DRAFT PROCEDURE TO OFFICIAL TRANSACTIONS OF US GOVERNMENT AGENCIES. WE PROPOSE TO PERMIT INDIVIDUALS TO OBTAIN THEIR LIRE THROUGH THIS SYSTEM OR TO PURCHASE THEIR LIRE FROM AUTHORIZED BANKS AND EXCHANGE DEALERS WITHIN

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TERMS OF ITALIAN EXCHANGE REGULATIONS.

9. FOLLOWING IS ENGLISH TEXT OF DRAFT LETTER FROM AMBASSADOR VOLPE TO MINISTER OF TREASURY COLOMBO AND ATTACHED ANNEX. COPIES IN ITALIAN HAVE BEEN PROVIDED ON INFORMAL BASIS TO BANK OF ITALY, EXCHANGE OFFICE AND MINISTRIES OF TREASURY AND FOREIGN TRADE, WHO HAVE GIVEN PROVISIONAL APPROVAL TO TEXTS.

10. QUOTE. DEAR MR. MINISTER: AS A RESULT OF THE VARIOUS CHANGES WHICH HAVE TAKEN PLACE IN THE FOREIGN EXCHANGE REGIME IN ITALY, ESPECIALLY THE CREATION AND SUBSEQUENT ABOLITION OF A MULTIPLE EXCHANGE RATE SYSTEM AND THE CONTINUATION OF A FLOATING RATE, PROBLEMS HAVE ARISEN IN APPLICATION OF THE "TASCA" AGREEMENT. THIS AGREEMENT CONCERNS THE DETERMINATION OF THE DOLLAR-LIRA RATE OF EXCHANGE TO BE APPLIED TO UNITED STATES GOVERNMENT EXPENDITURES IN ITALY AND THE PROCEDURES TO BE USED FOR PURCHASING LIRE FOR THESE PURPOSES. YOU MAY RECALL THAT THE TASCA AGREEMENT DATES FROM JANUARY 25, 1947 AND TOOK THE FORM OF AN EXCHANGE OF LETTERS BETWEEN THE THEN MINISTER OF THE TREASURY BERTONE AND MR. TASCA, THEN U.S. TREASURY REPRESENTATIVE AT THE AMERICAN EMBASSY IN ROME.

11. THE ANNEX TO THIS LETTER CONSTITUTES A PROPOSED NEW PROCEDURE TO REPLACE THE TASCA AGREEMENT WHICH WOULD PERMIT THE U.S. GOVERNMENT TO HAVE A FAVORABLE RATE OF EXCHANGE CONSISTENT WITH THE EXISTING FOREIGN EXCHANGE REGIME IN ITALY. IF YOU, MR. MINISTER, ARE IN AGREEMENT WITH THE ATTACHED PROPOSAL, YOUR LETTER OF ACKNOWLEDGMENT, TOGETHER WITH THIS LETTER AND ANNEX, WILL CONSTITUTE A NEW UNDERSTANDING SUPERSEDING THE PROVISIONS OF THE AGREEMENT OF JANUARY 25, 1947 (AS PREVIOUSLY AMENDED). SINCERELY YOURS, JOHN A. VOLPE.

12. ANNEX-PROCEDURE FOR FIXING THE EXCHANGE RATE AND FOR PURCHASING LIRE FOR U.S. GOVERNMENT EXPENDITURES IN ITALY  
PARAGRAPH 1. THE NORMAL WAY IN WHICH THE UNITED STATES GOVERNMENT WILL OBTAIN LIRE FOR U.S. GOVERNMENT EXPENDITURES WILL BE THROUGH PURCHASES FROM THE BANK  
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OF ITALY WITH PAYMENT MADE BY A DOLLAR CHECK DRAWN ON

THE U.S. TREASURY. THE APPLICABLE EXCHANGE RATE WILL BE THE PREVIOUS DAY'S AVERAGE OF THE OFFICIAL RATES OF EXCHANGE AT FIXING ON THE ROME AND MILAN STOCK EXCHANGES. HOWEVER, AT ITS OPTION THE U.S. GOVERNMENT MAY PURCHASE LIRE FROM THE BANK OF ITALY WITH PAYMENT IN U.S. BANKNOTES AT THE PREVIOUS DAY'S AVERAGE OF THE FIXING RATES FOR LARGE DENOMINATION DOLLAR BANKNOTES ON THE ROME AND MILAN STOCK EXCHANGE, ET OF A REIMBURSEMENT FEE FOR EXPENDITURES OF 0.1 PERCENT. PURCHASES OF LIRE MAY BE MADE BY U.S. GOVERNMENT CIVILIAN AND MILITARY DISBURSING OFFICERS FROM ANY OF THE BANK OF ITALY'S BRANCHES THROUGHOUT ITALY. PRIOR TO ANY CHANGE IN THE METHOD OF CALCULATING THE RATE OF EXCHANGE AS PROVIDED IN THIS PARAGRAPH, AN UNDERSTANDING SHALL BE REACH WITH RESPECT TO THE PROCEDURE TO BE USED IN THE IMPLEMENTATION OF THESE PROVISIONS.

13. PARAGRAPH 2. THE BANK OF ITALY BRANCHES WILL SUPPLY A STATEMENT TO DISBURSING OFFICERS AT THE TIME OF EACH LIRE/DOLLAR CONVERSION SHOWING THE AMOUNT OF LIRE DELIVERED, THE NUMBER OF DOLLARS GIVEN IN EXCHANGE AND THE RATE OF EXCHANGE AT WHICH THE LIRE IN QUESTION WERE SUPPLIED. IN ADDITION, THE BANK WILL PROVIDE TO THE AMERICAN EMBASSY IN ROME A MONTHLY REPORT OF THE TOTAL VOLUME OF DOLLAR/LIRA CONVERSIONS CARRIED OUT BY THE BANK AT EACH OF ITS BRANCHES.

14. PARAGRAPH 3. THE U.S. GOVERNMENT WILL PURCHASE ALL OF ITS LIRE FOR OFFICIAL EXPENDITURES IN ITALY FROM THE BANK OF ITALY IN ACCORDANCE WITH THE ABOVE PROCEDURES.

15. PARAGRAPH 4. IN THE EVENT THAT THERE SHOULD OCCUR A SUBSTANTIAL CHANGE IN ITALY'S FOREIGN EXCHANGE REGIME, PARTICULARLY AFFECTING THE EXCHANGE RATE SYSTEM, EITHER PARTY MAY REQUEST CONSULTATIONS IN ORDER TO DETERMINE WHETHER AND HOW THE PRESENT PROCEDURE SHOULD BE MODIFIED. END QUOTE. VOLPE. UNQUOTE  
STONE

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## Message Attributes

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